Stakeholder Comments on:
Straw Proposal for Modifying Rules Limiting Supply Bid Pool in IFM

Submitted by	Company	Submitted Date
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Southern California Edison "SCE" appreciates the opportunity to provide comments on the CAISO straw proposal on modification to the rules that limit the supply bid pool in the IFM, dated August 7, 2009. SCE views the current market design of limiting the supply bid pool in the IFM based on the CAISO's demand forecast as problematic. Both the market results on July 26, 2009, as well as continuing issues where units are economic based on IFM results, but nevertheless do not receive IFM awards because of the limited market power pool lead us to strongly support the CAISO's taking immediate interim steps. We recognize the implementation of the final FERC requirement of mitigating based on bid-in demand is nontrivial and will require material software changes. We encourage the CAISO to implement the FERC approach as soon as practical, but until that time an interim solution should be implemented.

The current design can create scenarios where the IFM market is unable to determine a solution without performing uneconomic adjustments of market schedules or unless it produces IFM solutions at clearly inflated price levels. This CAISO analysis of 7/26 demonstrates the current process resulted in needlessly inflated prices of around $500/MWh when something similar to the FERC bid-in demand process would have resulted in prices around $65/MWh. The current process is of particular concern since the CAISO may have plenty of economic resources available to serve willing market buyers, but these resources may not receive market awards, or even be allowed to participate in the IFM if they were not deemed "needed" based on the CAISO's forecast. Rather than relying on the CAISO's forecast to determine the supply pool that can receive market awards, the IFM pool should be determined economically based on the market desires to buy and to sell.

After reviewing the options in the CAISO whitepaper, SCE felt the need to offer an additional alternative. That is, several options proposed by the CAISO create the potential for bids to set prices in the IFM even if these bids have not been reviewed for potential market power mitigation (Option 1 & Option 2). Option 3 ensured that all bids were reviewed for market power prior to setting prices, but it had the potential to "over mitigate" resources if LMPM was cleared based on the total demand quantity bid into the IFM, even if these bids could had no reasonable chance of clearing the market.

As a result of these concerns, SCE proposed for consideration a 5th option with the following objectives:

- Emulate as closely as possible the FERC desired end-state solution, while keeping solution simple;
- Avoid economic supply from being excluded from participating in the IFM due to a disconnect between bid-in demand and the CAISO demand forecast;
- Maintain the principle design element that all CAISO bids eligible to set price in the IFM would first be reviewed for potential market power; and
- Avoid over-mitigating supply resources (as discussed by the CAISO in option 3).

SCE's proposal asks the CAISO to select a reasonable point on the bid-in demand curve to determine the quantity of demand used by the LMPM process only when this point exceeds the CAISO demand forecast. Using the maximum quantity of the CAISO's demand forecast or bid-in demand at some reasonable price level establishes an IFM pricing pool large enough to clear the IFM, while reviewing all bids for potential market power. A key element of our proposal is to determine the demand quantity to be used in the LMPM process. While not an exhaustive list of potential methodologies that could be adopted we proposed the following options:

- Proxy peaker costs indexed to daily gas prices,
- LAP demand quantity bid a some percentage of the cap,
- Demand quantity bid at a reasonable price in similar conditions, historic price or forecast price,
- Fix percentage of the CAISO demand forecast to be used in all instances where bid-in and demand exceeds the CAISO's forecast by some threshold.

SCE views our proposal as a somewhat simple approach in achieving a result that closely mimics the end-state market design rules required by FERC, until such a time as the final design can be implemented. It is our opinion that our proposal strikes a balance between making available sufficient economic supply to participate in the IFM while reviewing all bids passed to the IFM for potential market power.

That being said, we now recognize the CAISO feels our approach requires software changes, and this would necessarily delay implementation. Further, the CAISO indicates the current software already has a "flag" that allows it to pass all bids to the IFM. While SCE has concerns over passing un-reviewed bids to the IFM pricing runs (and we do not support this approach as permanent policy), we have concrete results that demonstrate the shortcomings of the current process and the need for some form of interim action while we await the more robust solution.

We are hopeful the CAISO will determine the SCE solution can be implemented quickly and without software changes. However, if the CAISO determines the only viable and effective action for addressing this issue expeditiously is to pass all bids to the IFM, SCE would support this approach as an interim solution under the following conditions:

1) The proposal is implemented quickly. The CAISO should expedite implementation of this request at FERC. If delay is inevitable, we should instead implement a solution that reviews bids for market power prior to passing them to the IFM pricing runs.
2) DMM and the CAISO commitment to monitoring the market impacts of passing un-reviewed bids to the IFM. We remain concerned that market power issue may arise based on bid-in demand and that market power may be exercised.
3) In the event CAISO/DMM identifies market power problems with un-reviewed bids, the CAISO must have a plan to take corrective action. This could include moving to a second phase of changes consisting of SCE's proposal, or better yet the FERC end-state solution, or some other form of mitigation applied to the un-reviewed bids. For example, rather than forwarding all bids to the IFM, the CAISO could only forward bids from units that voluntarily agree to mitigation in exchange for the right to be forwarded to the IFM pricing pool outside of the market power runs.

In sum, SCE strongly supports the CAISO taking immediate interim actions to address this issue. While we are hopeful some variation of our proposal can be implemented quickly, if this is simply not technically feasible, the CAISO should immediately move forward with a technically feasible and effective interim approach.